



**CITY OF ANAHEIM
WATER UTILITY FUND**

Financial Statements

June 30, 2010 and 2009

(With Independent Auditors' Report Thereon)

**CITY OF ANAHEIM
WATER UTILITY FUND**

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KPMG LLP
Suite 700
20 Pacifica
Irvine, CA 92618-3391

Independent Auditors' Report

The Honorable City Council
City of Anaheim, California:

We have audited the accompanying financial statements of the Water Utility Fund (Water Utility) of the City of Anaheim, California (the City), as of and for the years ended June 30, 2010 and 2009, as listed in the accompanying table of contents. These financial statements are the responsibility of the City's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Water Utility's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in note 1 to the financial statements, the financial statements present only the Water Utility Fund of the City of Anaheim, California and do not purport to, and do not, present fairly the financial position of the City, as of June 30, 2010 and 2009, and changes in its financial position and its cash flows, where applicable, for the years then ended, in conformity with U.S. generally accepted accounting principles.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Water Utility Fund of the City of Anaheim, California, as of June 30, 2010 and 2009, and the changes in its financial position and its cash flows for the years then ended, in conformity with U.S. generally accepted accounting principles.

Management's discussion and analysis on pages 3 through 14 is not a required part of the basic financial statements but is supplementary information required by U.S. generally accepted accounting principles. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

KPMG LLP

Orange County, California
December 14, 2010

**CITY OF ANAHEIM
WATER UTILITY FUND**

Management's Discussion and Analysis

(Unaudited)

June 30, 2010 and 2009

(In thousands)

As management of Anaheim Public Utilities, a department of the City of Anaheim, California (City), we offer the readers of the City of Anaheim Water Utility Fund (Water Utility) financial statements a narrative overview and analysis of the financial statements for the fiscal years ended June 30, 2010 and 2009. We encourage readers to consider the information presented here in conjunction with the accompanying financial statements. All amounts, unless otherwise indicated, are expressed in thousands of dollars.

Financial Highlights

The assets of the Water Utility exceeded its liabilities at the close of fiscal years 2010 and 2009 by \$233,244 and \$232,170, respectively. Of these amounts, \$13,057 and \$20,229, respectively, were available to meet the Water Utility's ongoing obligations to creditors and customers (unrestricted fund net assets). The Water Utility's total fund net assets increased by \$1,074 (0.5%) and decreased by \$134 (0.1%) for the fiscal years ended June 30, 2010 and 2009, respectively. Unrestricted fund net assets represented 24.5% and 43.0% of annual operating expenses for fiscal years 2010 and 2009, respectively.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the Water Utility's financial statements. Because the Water Utility is a business-type activity of the City, an enterprise fund is used to account for its operations. These financial statements include only the activities of the Water Utility and provide comparative information for the last two fiscal years. Information on citywide financial results is available in the City's Comprehensive Annual Financial Report as of June 30, 2010.

The Water Utility's financial statements comprise two components: 1) financial statements and 2) notes to the financial statements. Included as part of the financial statements are the balance sheets, statements of revenues, expenses, and changes in fund net assets, and statements of cash flows.

The balance sheets present the assets and liabilities with the difference between the two reported as fund net assets. Over time, increases or decreases in fund net assets may serve as a useful indicator of whether the financial condition of the Water Utility is improving or deteriorating.

The statements of revenues, expenses, and changes in fund net assets present information showing how the Water Utility's fund net assets have changed during the most recent two fiscal years. Results of operations are recorded using the accrual basis of accounting, whereby transactions are reported as underlying events occur, regardless of the timing of cash flows. Thus, revenues and expenses are reported in these statements for some items that will result in cash flows in future fiscal periods, such as accounts receivable and accounts payable. The accrual basis of accounting is more fully described in the accompanying notes to financial statements.

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The statements of cash flows present the flows of cash and cash equivalents during the last two fiscal years, including certain restricted amounts.

The notes to financial statements provide additional information that is essential to the full understanding of the data provided in the financial statements.

Financial Analysis

As noted earlier, fund net assets may serve over time as a useful indicator of the Water Utility's financial position. In the case of the Water Utility, assets exceed liabilities by \$233,244 and \$232,170 at June 30, 2010 and 2009, respectively.

A large portion of the Water Utility's fund net assets (92.8% and 89.5% as of June 30, 2010 and 2009, respectively) reflects its investment in capital assets, such as production, transmission, distribution facilities, and general plant, less any related debt used to acquire those assets that remain outstanding. The Water Utility uses these capital assets to provide services to customers. Consequently, these assets are not available for future spending. Resources needed to repay the outstanding debt on the balance sheets must come from other sources such as operations.

An additional portion of the Water Utility's fund net assets (1.6% and 1.8% as of June 30, 2010 and 2009, respectively) represents resources that are subject to external restrictions on how they may be used. These restrictions are for items such as debt repayment and other legally restricted purposes. The unrestricted portion of the Water Utility's fund net assets (5.6% and 8.7% as of June 30, 2010 and 2009, respectively) may be used to meet the Water Utility's ongoing obligations to creditors and customers. The Water Utility's condensed balance sheets at June 30 are as follows:

Condensed Balance Sheets

	<u>2010</u>	<u>2009</u>	<u>2008</u>
Current and other assets	\$ 41,774	60,393	41,041
Net utility plant	273,853	258,456	233,674
Total assets	<u>315,627</u>	<u>318,849</u>	<u>274,715</u>
Long-term liabilities, net of current portion	62,455	64,141	17,951
Current liabilities	19,928	22,538	24,460
Total liabilities	<u>82,383</u>	<u>86,679</u>	<u>42,411</u>
Invested in capital assets, net of related debt	216,360	207,826	215,762
Restricted	3,827	4,115	3,809
Unrestricted	13,057	20,229	12,733
Total fund net assets	<u>\$ 233,244</u>	<u>232,170</u>	<u>232,304</u>

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WATER UTILITY FUND**

Management's Discussion and Analysis

(Unaudited)

June 30, 2010 and 2009

(In thousands)

As of June 30, 2010

Assets

Total assets as of June 30, 2010 and 2009 were \$315,627 and \$318,849, respectively. The \$3,222 (1.0%) decrease in total assets is due primarily to a \$9,782 decrease in current assets, partially offset by a \$6,560 increase in noncurrent assets. Current assets decreased 22.9% primarily because \$20,948 of cash and cash equivalents were used for current year capital purchases. See the statements of cash flows for additional information regarding changes in cash and cash equivalents. Noncurrent assets increased 2.4% primarily as a result of increases in net utility plant. The \$15,397 (6.0%) increase in net utility plant resulted from the Water Utility building additional storage facilities, wells, and distribution facilities under a plan to ensure the water supply continues to be safe, reliable, and sufficient to meet future demands.

Liabilities

Total liabilities as of June 30, 2010 and 2009 were \$82,383 and \$86,679, respectively. The \$4,296 (5.0%) decrease in total liabilities is due to a \$1,911 decrease in current liabilities, a \$699 decrease in restricted current liabilities, and a \$1,686 decrease in long-term liabilities. Current liabilities decreased by 9.9% primarily because of a \$1,220 decrease in regulatory credits resulting from the recognition of rate stabilization account (RSA) revenue. See note 8 to the financial statements for additional information regarding the Utility's regulatory credits. Long-term liabilities decreased 2.6% primarily as a result of current year payments of principal on long-term debt.

Fund Net Assets

Total fund net assets as of June 30, 2010 and 2009 were \$233,244 and \$232,170, respectively. Total fund net assets increased by \$1,074 (0.5%) during fiscal year 2010. Fund net assets invested in capital assets, net of related debt increased \$8,534 (4.1%) due to the continued expansion and refurbishment of water transmission and distribution infrastructure. Unrestricted net assets decreased \$7,172 (35.5%), because available cash and investments were used to fund these ongoing capital construction projects.

As of June 30, 2009

Assets

Total assets as of June 30, 2009 and 2008 were \$318,849 and \$274,715, respectively. The \$44,134 (16.1%) increase in total assets is due primarily to a \$38,559 increase in noncurrent assets, and a \$5,575 increase in current assets. Noncurrent assets increased 16.2% as a result of increases in net utility plant and in restricted assets. The \$24,782 (10.6%) increase in net utility plant resulted from the Water Utility building additional storage facilities, wells, and distribution facilities under a plan to ensure the water supply continues to be safe, reliable, and sufficient to meet future demands. Restricted

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(Unaudited)

June 30, 2010 and 2009

(In thousands)

assets increased by \$13,470 (384.2%) primarily because some proceeds from the debt financing obtained to fund these planned utility plant additions remained unspent as of June 30, 2009.

Liabilities

Total liabilities as of June 30, 2009 and 2008 were \$86,679 and \$42,411, respectively. The \$44,268 (104.4%) increase in total liabilities is due to a \$46,190 increase in long-term liabilities, which was offset by a \$1,922 decrease in current liabilities. Long-term liabilities increased 257.3% primarily due to the issuance of \$48,580 Water Revenue Bonds used to finance the capital projects program for improving and safeguarding the Water Utility's water supply infrastructure.

Fund Net Assets

Total fund net assets as of June 30, 2009 and 2008 were \$232,170 and \$232,304, respectively. Total fund net assets decreased by \$134 (0.1%) during fiscal year 2009. Fund net assets invested in capital assets, net of related debt decreased \$7,936 (3.7%) primarily because the issuance of the \$48,580 new Water Revenue Bonds offset the construction additions to the utility plant during the year. Unrestricted net assets increased \$7,496 (58.9%), because the reduction in current liabilities enabled additional cash and investments to become available.

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Management's Discussion and Analysis

(Unaudited)

June 30, 2010 and 2009

(In thousands)

The Water Utility's statements of revenues, expenses, and changes in fund net assets for the years ended June 30 are summarized as follows:

Revenues, Expenses, and Changes in Fund Net Assets

	<u>2010</u>	<u>2009</u>	<u>2008</u>
Revenues:			
Sale of water, net	\$ 54,449	49,985	47,938
RSA Revenues	1,300	—	—
Other operating revenues	619	822	1,185
Interest income	1,111	2,218	1,927
Other nonoperating revenues	308	14	2
Capital contributions	713	1,199	3,005
Total revenues	<u>58,500</u>	<u>54,238</u>	<u>54,057</u>
Expenses:			
Purchased water	27,227	22,558	21,608
Treatment and pumping	6,448	6,747	6,650
Operations, maintenance, and administration	11,556	10,818	12,932
Depreciation	8,103	6,918	7,616
Interest expense	1,746	1,612	313
Total expenses	<u>55,080</u>	<u>48,653</u>	<u>49,119</u>
Transfers:			
Transfer to the General Fund of the City	(2,380)	(4,062)	(2,008)
Transfer of right-of-way fee to the City	(750)	(719)	(721)
Transfers from other funds of the City	963	407	—
Transfers to other funds of the City	(179)	(1,345)	(16)
Total transfers	<u>(2,346)</u>	<u>(5,719)</u>	<u>(2,745)</u>
Changes in fund net assets	1,074	(134)	2,193
Fund net assets at beginning of year	<u>232,170</u>	<u>232,304</u>	<u>230,111</u>
Fund net assets at end of year	<u>\$ 233,244</u>	<u>232,170</u>	<u>232,304</u>

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WATER UTILITY FUND**

Management's Discussion and Analysis

(Unaudited)

June 30, 2010 and 2009

(In thousands)

Revenues

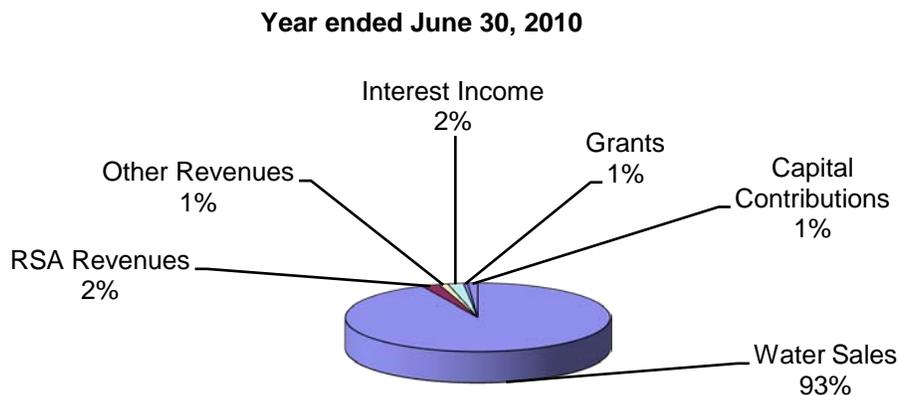
Year ended June 30, 2010

Total revenues for the fiscal year ended June 30, 2010 were \$58,500 as compared with \$54,238 in fiscal year 2009, an increase of \$4,262. This increase was primarily due to a \$4,464 increase in revenues from the sale of water. Revenues from the sale of water increased 8.9% primarily as a result of a 21.2% increase in the Water Commodity Adjustment (WCA) charge billed to customers beginning July 7, 2009. The WCA charge is a rate charged to all consumers that can be adjusted annually to recover the changes in the cost of water. In fiscal year 2010, the costs of purchased water increased substantially, primarily as a result of a 21.1% increase in the per unit cost of treated water and a 17.5% increase in the per unit cost of untreated water purchased from the Metropolitan Water District (MWD) of Southern California. In addition, effective July 7, 2009, the Utility began charging customers 7.5 cents per hundred cubic foot for the Water System Reliability Adjustment (WSRA) to recover projected capital costs, including rehabilitation and construction of water and reclaimed water system infrastructure, and related debt service payments.

Year ended June 30, 2009

Total revenues for the fiscal year ended June 30, 2009 were \$54,238 as compared with \$54,057 in fiscal year 2008. There were no significant or unusual changes.

Revenues by Source



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WATER UTILITY FUND**

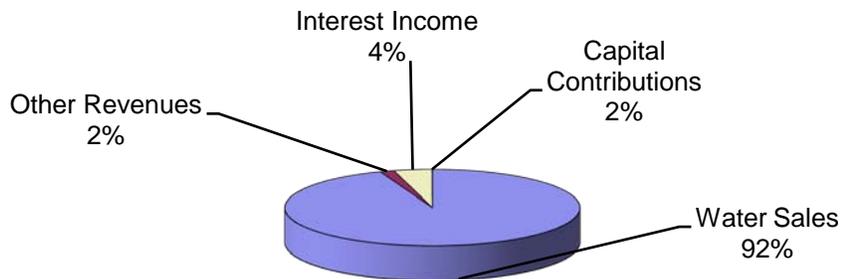
Management's Discussion and Analysis

(Unaudited)

June 30, 2010 and 2009

(In thousands)

Year ended June 30, 2009



Expenses

Year ended June 30, 2010

Total expenses for the fiscal year ended June 30, 2010 were \$55,080 as compared with \$48,653 in fiscal year 2009. This \$6,427 (13.2%) increase in total expenses is primarily due to a \$4,669 increase in purchased water costs. The cost of purchased water increased 20.7%, primarily because of higher per unit costs imposed by MWD, one of the two primary water supply sources for the Water Utility. During the fiscal year 2010, MWD's per unit costs increased by 19.6%. In addition, the Utility's other water supply source, the Orange County Water District (OCWD), reduced its allowable Basin Production Percentage (BPP) from 69% to 64%, thus requiring the Utility to purchase more water from MWD at the higher cost.

Year ended June 30, 2009

Total expenses for the fiscal year ended June 30, 2009 were \$48,653 as compared with \$49,119 in fiscal year 2008. This \$466 (0.9%) decrease in total expenses is due to a \$2,114 decrease in operations, maintenance, and administrative expenses (OM&A), partially offset by a \$97 increase in treatment and pumping costs, and a \$950 increase in purchased water costs, and a \$1,299 increase in interest expense.

OM&A decreased 16.3% from fiscal year 2008. Administrative costs decreased by \$2,469 (116.8%), maintenance costs decreased by \$179 (8.5%), and operating costs increased by \$534 (25.3%) over the prior year. Administrative costs decreased because increasing amounts of administrative overhead costs became eligible for capitalization as a result of the expansion of the Water Utility's capital improvement program. Maintenance costs also decreased due to the increasing capital projects workload being performed to ensure system reliability.

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(Unaudited)

June 30, 2010 and 2009

(In thousands)

The cost of purchased water increased 4.4%, primarily because of higher per unit costs imposed by both OCWD and the MWD, the two primary water supply sources for the Water Utility. Treatment and pumping costs also increased by 1.5% primarily as a result of increased pump power (electricity) costs.

The large (415.0%) increase in interest expense resulted from the additional interest payments made on the \$48,580 Water Revenue Bonds issued in July 2008.

Transfers

Year ended June 30, 2010

Transfers to the City's General Fund, as defined by City Charter, are equal to a maximum of 4.0% of total operating revenues. The transfer to the City's General Fund was \$2,380 for fiscal year 2010. The decrease of \$1,682 was mainly due to a one-time additional transfer of \$2,084 to the General Fund of the City in fiscal year 2009.

In addition, a right-of-way fee is transferred to the City's General Fund and is equal to 1.5% of net revenues of the prior fiscal year. Net revenues are defined as revenues from sale of water less uncollectible accounts. The right-of-way fee transferred to the City amounted to \$750 for fiscal year 2010. There were no significant changes in the amount of right-of-way fee transferred to the City during fiscal year 2010 when compared with fiscal year 2009.

Transfers in from other funds amounted to \$963 in fiscal year 2010 and resulted from the transfer of vehicle capital assets at their net book value from the City to the Water Utility.

Year ended June 30, 2009

Transfers to the City's General Fund, as defined by City Charter, are equal to a maximum of 4% of total operating revenues. In order to match the transfer's revenue base to the time period in which the revenues are earned, the Water Utility made a one-time additional transfer of \$2,084 to the General Fund of the City, which is based on the current year's total operating revenues. The total transfer to the City's General Fund was \$4,062 for fiscal year 2009.

The transfer of the right-of-way fee to the City is equal to 1.5% of net revenues from the sale of water in the prior fiscal year. Net revenues are defined as revenues from sale of water less uncollectible accounts. The right-of-way fee transferred to the City was \$719 for fiscal year 2009. There were no significant changes in the amount of right-of-way fee transferred to the City during fiscal year 2009 when compared with fiscal year 2008.

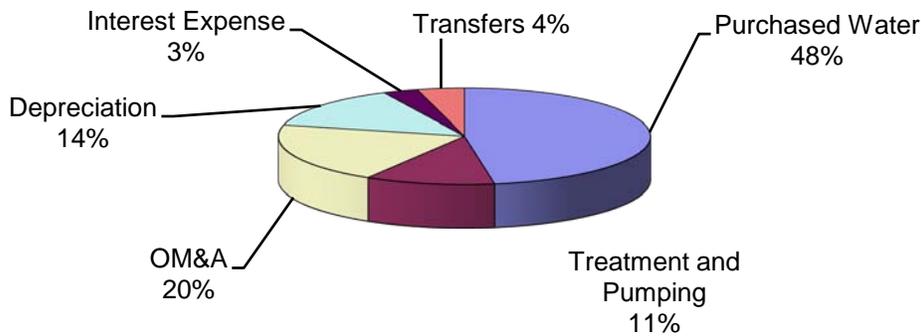
Upon the completion of several joint capital projects, the Water Utility transferred ownership of its share of these projects, valued at \$1,345, to the Electric Utility.

**CITY OF ANAHEIM
WATER UTILITY FUND**

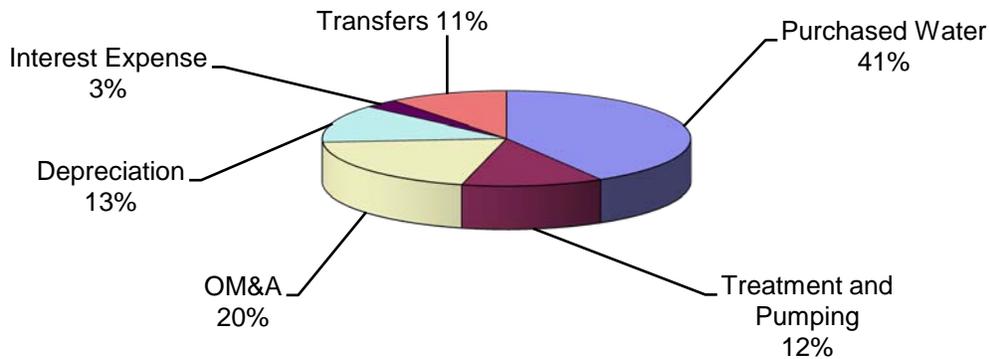
Management's Discussion and Analysis
(Unaudited)
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(In thousands)

Expenses and Transfers

Year ended June 30, 2010



Year ended June 30, 2009



Capital Assets and Debt Administration

Capital Assets

The Water Utility's net investment in capital assets as of June 30, 2010 and 2009 was \$273,853 and \$258,456, respectively, net of accumulated depreciation. The Water Utility's net investment in capital assets includes land, production wells and treatment plant, transmission and distribution facilities, and general plant. The total net additions to investment in capital assets (before accumulated depreciation) for fiscal year 2010 were \$23,097 (6.6%).

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WATER UTILITY FUND**

Management's Discussion and Analysis

(Unaudited)

June 30, 2010 and 2009

(In thousands)

The Water Utility's investments in capital assets as of June 30 are as follows:

	<u>2010</u>	<u>2009</u>	<u>2008</u>
Source of water supply	\$ 37,446	37,446	35,900
Pumping plant	41,934	41,874	40,482
Transmission and distribution	249,713	244,018	217,356
General plant	6,301	4,030	4,908
Land	2,298	2,298	2,130
Construction in progress	36,413	21,342	21,409
Total utility plant	374,105	351,008	322,185
Less accumulated depreciation	<u>(100,252)</u>	<u>(92,552)</u>	<u>(88,511)</u>
Net utility plant	<u>\$ 273,853</u>	<u>258,456</u>	<u>233,674</u>

Additional information on the Water Utility's capital assets can be found in note 3 to the financial statements.

As of June 30, 2010

The Water Utility showed a net increase of \$15,397 (6.0%) in the investment in capital assets (net utility plant) this fiscal year, due mainly to ongoing projects to expand and refurbish the water transmission and distribution infrastructure and source of supply. In 1999, the Water Utility made the decision to increase its pumping capacity by building ten new wells over the next decade. As of June 30, 2010, the Water Utility has completed approximately 80% of the planned new well pumping capacity.

As of June 30, 2009

The Water Utility showed a net increase of \$24,782 (10.6%) in the investment in capital assets (net utility plant) this fiscal year, due mainly to ongoing projects to expand and refurbish the water transmission and distribution infrastructure and source of supply. In 1999, the Water Utility made the decision to increase its pumping capacity by building one new well per year for each of the subsequent 10 years. As of June 30, 2009, the Water Utility has completed approximately 80% of the planned new well pumping capacity.

Long-Term Debt

As of June 30, 2010 and 2009, the Water Utility had total long-term debt outstanding of \$64,628 and \$67,080, respectively.

**CITY OF ANAHEIM
WATER UTILITY FUND**

Management's Discussion and Analysis

(Unaudited)

June 30, 2010 and 2009

(In thousands)

The Water Utility's outstanding long-term debt as of June 30 is as follows:

	<u>2010</u>	<u>2009</u>	<u>2008</u>
Water revenue bonds	\$ 53,010	54,500	7,355
Notes payable and advances	11,618	12,580	13,515
Total long-term debt outstanding	64,628	67,080	20,870
Less:			
Current portion	(1,779)	(2,452)	(2,370)
Unamortized bond premium	17	41	122
Unamortized refunding costs	(411)	(528)	(671)
Total noncurrent long-term debt outstanding	\$ <u>62,455</u>	<u>64,141</u>	<u>17,951</u>

The Water Utility maintains an AAA credit rating from Standard & Poor's. Additional information on the Water Utility's long-term debt can be found in note 5 to the financial statements.

As of June 30, 2010

Long-term debt decreased \$1,686 (2.6%) primarily due to the repayment of principal on outstanding bonds and notes payable and advances. The revenues of the Water Utility have been pledged to pay the outstanding long-term debt.

As of June 30, 2009

Long-term debt increased \$46,210 (221.4%) primarily due to the issuance of \$48,580 Water Revenue Bonds, the proceeds of which provided funding for the Water Utility's ongoing improvements to the Water Utility's infrastructure system. The revenues of the Water Utility have been pledged to pay the outstanding long-term debt. The Water Utility continued to make repayments of principal on outstanding bonds and notes payable in accordance with the applicable payment terms.

Economic Factors and Rates

For fiscal year 2011, the OCWD set the Basin Production Percentage (BPP) for all cities and water districts they serve (including Anaheim) at 62.0%. The Water Utility will need to purchase the remainder of its water supply requirements from MWD. Water purchased from MWD is priced higher than ground water pumped from OCWD. The Water Utility's Water Rates, Rules, and Regulations provide for an automatic adjustment of its commodity adjustment when OCWD and MWD increase the cost per acre foot of water. Effective July 1, 2010, the Water Commodity Adjustment increased from \$1.20 to \$1.22 per 100 cubic foot.

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June 30, 2010 and 2009

(In thousands)

In addition, as approved on March 18, 2008, the Water Utility instituted a charge to all customers for a Water System Reliability Adjustment (WSRA). The WSRA is set to \$0.15 per 100 cubic foot, effective July 1, 2010. The purpose of this charge is to recover projected capital costs, including rehabilitation and construction of water and reclaimed water system infrastructure and the related debt service payments.

Requests for Information

This financial report is designed to provide a general overview of the Water Utility's finances. Questions concerning any information provided in this report or requests for additional financial information should be addressed to the Assistant General Manager – Finance and Administration, Anaheim Public Utilities, 201 South Anaheim Boulevard, Suite 1101, Anaheim, CA 92805.

**CITY OF ANAHEIM
WATER UTILITY FUND**

Balance Sheets

June 30, 2010 and 2009

(In thousands)

Assets	2010	2009
Utility plant:		
Source of water supply	\$ 37,446	37,446
Pumping plant	41,934	41,874
Transmission and distribution	249,713	244,018
General plant	6,301	4,030
Total depreciable utility plant	<u>335,394</u>	<u>327,368</u>
Less accumulated depreciation	<u>(100,252)</u>	<u>(92,552)</u>
Net depreciable utility plant	235,142	234,816
Land	2,298	2,298
Construction in progress	36,413	21,342
Net utility plant	<u>273,853</u>	<u>258,456</u>
Restricted assets:		
Restricted cash and cash equivalents	1,099	980
Investments	7,155	15,996
Total restricted assets	<u>8,254</u>	<u>16,976</u>
Other assets:		
MWDOC pipeline receivable	133	210
Unamortized debt issuance costs	402	440
Total other assets	<u>535</u>	<u>650</u>
Total noncurrent assets	<u>282,642</u>	<u>276,082</u>
Current assets:		
Cash and cash equivalents	7,227	6,951
Investments	14,692	24,405
Restricted cash and cash equivalents	1,524	1,094
Restricted investments	1,048	2,177
Accounts receivable, net	6,747	6,488
Accrued interest receivable	180	213
Interfund receivable	15	—
Materials and supplies inventory	371	320
Purchased water in storage	1,181	1,119
Total current assets	<u>32,985</u>	<u>42,767</u>
Total assets	<u>\$ 315,627</u>	<u>318,849</u>

**CITY OF ANAHEIM
WATER UTILITY FUND**

Balance Sheets

June 30, 2010 and 2009

(In thousands)

Fund Net Assets and Liabilities	2010	2009
Fund net assets:		
Invested in capital assets, net of related debt	\$ 216,360	207,826
Restricted for:		
Debt service	1,088	1,530
Renewal and replacement	2,739	2,585
Unrestricted	13,057	20,229
Total fund net assets	233,244	232,170
Long-term liabilities:		
Long-term debt obligations, less current portion	62,455	64,141
Total long-term liabilities	62,455	64,141
Current liabilities (payable from restricted assets):		
Current portion of long-term debt	1,779	2,452
Arbitrage rebate liability	3	2
Accrued interest payable	790	817
Total current liabilities (payable from restricted assets)	2,572	3,271
Current liabilities (payable from unrestricted current assets):		
Accounts payable and accrued expenses	10,285	10,987
Wages payable	321	277
Regulatory credits	5,937	7,157
Customer deposits	813	846
Total current liabilities (payable from unrestricted current assets)	17,356	19,267
Total liabilities	82,383	86,679
Total fund net assets and liabilities	\$ 315,627	318,849

See accompanying notes to financial statements.

**CITY OF ANAHEIM
WATER UTILITY FUND**

Statements of Revenues, Expenses, and Changes in Fund Net Assets

Years ended June 30, 2010 and 2009

(In thousands)

	2010	2009
Operating revenues:		
Sales of water, net	\$ 54,449	49,985
RSA Revenues	1,300	—
Other operating revenues	619	822
	<u>56,368</u>	<u>50,807</u>
Total operating revenues		
Operating expenses:		
Purchased water	27,227	22,558
Treatment and pumping	6,448	6,747
Operations, maintenance, and administration	11,556	10,818
Depreciation	8,103	6,918
	<u>53,334</u>	<u>47,041</u>
Total operating expenses		
Operating income	<u>3,034</u>	<u>3,766</u>
Nonoperating revenues (expenses):		
Interest income	1,111	2,218
Interest expense	(1,746)	(1,612)
Grants	308	14
	<u>(327)</u>	<u>620</u>
Total net nonoperating revenues		
Income before capital contributions and transfers	<u>2,707</u>	<u>4,386</u>
Capital contributions	713	1,199
Transfer to the General Fund of the City	(2,380)	(4,062)
Transfer of right-of-way fee to the City	(750)	(719)
Transfers from other funds of the City	963	407
Transfers to other funds of the City	(179)	(1,345)
	<u>1,074</u>	<u>(134)</u>
Change in fund net assets		
Fund net assets at beginning of year	<u>232,170</u>	<u>232,304</u>
Fund net assets at end of year	<u>\$ 233,244</u>	<u>232,170</u>

See accompanying notes to financial statements.

**CITY OF ANAHEIM
WATER UTILITY FUND**

Statements of Cash Flows

Years ended June 30, 2010 and 2009

(In thousands)

	2010	2009
Cash flows from operating activities:		
Receipts from customers and users	\$ 54,545	49,881
Receipts from services provided to other funds of the City	311	248
Payments to suppliers	(28,974)	(27,251)
Payments to employees	(12,616)	(11,503)
Payments for services provided by other funds of the City	(4,412)	(4,516)
Net cash provided by operating activities	8,854	6,859
Cash flows from noncapital financing activities:		
Transfers to the General Fund and other funds of the City	(3,130)	(4,781)
Transfers from other funds of the City	—	407
Receipts from grants	308	14
Net cash used in noncapital financing activities	(2,822)	(4,360)
Cash flows from capital and related financing activities:		
Proceeds from borrowings, net of discount	—	48,532
Issuance costs	—	(374)
Capital purchases	(20,948)	(29,812)
Principal payments on long-term debt	(2,452)	(2,370)
Interest paid	(2,900)	(2,355)
Transfers to other funds of the City for capital purposes	(50)	(590)
Capital contributions	239	—
Net cash provided by (used in) capital and related financing activities	(26,111)	13,031
Cash flows from investing activities:		
Purchases of investment securities	(1,188)	(80,913)
Proceeds from sale and maturity of investment securities	21,031	61,973
Collection of pipeline receivable	77	24
Interest income received	984	2,107
Net cash provided by (used in) investing activities	20,904	(16,809)
Increase (decrease) in cash and cash equivalents	825	(1,279)
Cash and cash equivalents at beginning of year	9,025	10,304
Cash and cash equivalents at end of year	\$ 9,850	9,025

**CITY OF ANAHEIM
WATER UTILITY FUND**

Statements of Cash Flows

Years ended June 30, 2010 and 2009

(In thousands)

	2010	2009
Reconciliation of operating income to net cash provided by operating activities:		
Operating income	\$ 3,034	3,766
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	8,103	6,918
Changes in assets and liabilities:		
Accounts receivable, net	(259)	(150)
Materials and supplies inventory	(51)	(36)
Purchased water in storage	(62)	(1,087)
Accounts payable and accrued expenses	(702)	(2,056)
Wages payable	44	32
Customer deposits	(33)	(731)
Regulatory credits	(1,220)	203
Total adjustments	5,820	3,093
Net cash provided by operating activities	\$ 8,854	6,859
Schedule of noncash investing, capital, and financing activities:		
Capital contributions	\$ 459	1,199
Transfers in capital assets	963	—
Transfers out of capital assets	(129)	(755)
Increase in fair value of investments	160	194
Reconciliation of cash and cash equivalents:		
Cash and cash equivalents	\$ 7,227	6,951
Restricted cash and cash equivalents, current portion	1,524	1,094
Restricted cash and cash equivalents, noncurrent portion	1,099	980
Total cash and cash equivalents	\$ 9,850	9,025

See accompanying notes to financial statements.

**CITY OF ANAHEIM
WATER UTILITY FUND**

Notes to Financial Statements

June 30, 2010 and 2009

(In thousands)

(1) Summary of Significant Accounting Policies

(a) Basis of Accounting

The Water Utility Fund (Water Utility) of the City of Anaheim, California (City) was established on June 30, 1971, at which time the portion of the City's General Fund net assets related to water system operations was transferred to Water Utility net assets. The financial statements of the Water Utility, an enterprise fund, are presented on the accrual basis of accounting in conformity with U.S. generally accepted accounting principles and accounting principles and methods prescribed by the California Public Utilities Commission (CPUC). The Water Utility is not subject to the regulations of the CPUC. Under Governmental Accounting Standards Board Statement No. 20, *Accounting and Financial Reporting for Proprietary Fund and Other Governmental Entities That Use Proprietary Fund Accounting*, the Water Utility has elected not to apply Financial Accounting Standards Board (FASB) pronouncements issued after November 30, 1989.

(b) New Accounting Pronouncements

On July 1, 2009, the Water Utility adopted the following new accounting pronouncements issued by the Governmental Accounting Standards (GASB):

- Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*. This Statement requires the Water Utility to report intangible assets as part of the capital assets. Implementation of this Statement had no material effect on amounts reported in the Water Utility's financial statements for the year ended June 30, 2010.
- Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*. This Statement requires the Water Utility to report its derivative instruments at fair value. Changes in fair value for effective hedges are to be reported as deferrals on the balance sheet, changes in fair value of derivative instruments not meeting the criteria for an effective hedge, or that are associated with investments are to be reported in the investment section of the statement of revenues, expenses and changes in fund net assets. Implementation of this statement had no material effect on amounts reported in the Water Utility's financial statements for the year ended June 30, 2010.

(c) Utility Plant and Depreciation

The cost of additions to utility plant and replacement of retired units is capitalized. Utility plant is recorded at cost, including capitalized interest, or in the case of contributed plant at fair market value at the date of the contribution, except those assets acquired prior to July 1, 1977, which are recorded at historical cost. Cost includes labor, materials, allocated indirect charges such as engineering, supervision, construction and transportation equipment, retirement plan contributions and other fringe benefits, and certain administrative and general expenses. The cost of minor replacements is included in

**CITY OF ANAHEIM
WATER UTILITY FUND**

Notes to Financial Statements

June 30, 2010 and 2009

(In thousands)

maintenance expense. The net book value of assets retired or disposed of, related salvage value proceeds and the costs of removal are recorded in accumulated depreciation.

Depreciation of utility plant is provided by the straight-line method based on the following estimated service lives of the properties:

Source of water supply	15 to 75 years
Pumping plant	10 to 75 years
Transmission and distribution	20 to 75 years
General plant	5 to 50 years

(d) Pooled Cash and Investments

The City pools available cash from all funds for the purpose of enhancing investment income through investment activities. Investments in U.S. Treasury obligations, U.S. agency securities, and corporate notes are carried at fair value based on quoted market prices. Participating guaranteed investment contracts and flexible repurchase agreements are carried at fair value based on net realizable value. Money market mutual funds are carried at fair value based on the fund's share price. The City's investment in the State of California Local Agency Investment Fund (LAIF) is carried at fair value based on the value of each participating dollar as provided by LAIF. LAIF is authorized by California Government Code (Government Code) Section 16429 under the oversight of the Treasurer of the State of California. Commercial paper, nonparticipating guaranteed investment contracts, and negotiable certificates of deposit are carried at amortized cost (which approximates fair value). Investment income, which includes changes in fair value, is allocated to all funds on the basis of average daily cash and investment balances. The Water Utility's cash and investments pooled with the City Treasurer (Treasurer) are carried at fair value based on the value of each participating dollar. See note 2 for further discussion.

For the purpose of the statements of cash flows, the Water Utility considers cash equivalents to be highly liquid short-term investments that are readily convertible to known amounts of cash and mature within three months from the date they are acquired. Cash and cash equivalents are included in the City's cash and investments pool and in accounts held by fiscal agents.

(e) Revenue Recognition

Revenue is recorded in the period earned. The Water Utility accrues estimated unbilled revenues for water sold but not billed at the end of a fiscal period, which amounted to approximately \$3,816 and \$3,825 for fiscal years 2010 and 2009, respectively. Residential and smaller commercial accounts are billed bimonthly, and all other customers are billed monthly.

**CITY OF ANAHEIM
WATER UTILITY FUND**

Notes to Financial Statements

June 30, 2010 and 2009

(In thousands)

The City Council must be notified for all changes in base water rates. Rates have been structured to recover the Water Utility's costs for providing water services. The Water Utility's Rates, Rules, and Regulations include a Water Commodity Adjustment formula by which billings to customers are subject to adjustment, up or down, to reflect variations in the cost of water production and water quality measures to the Water Utility.

Revenues are reported net of uncollectible amounts. Total uncollectible amounts written off are \$91 and \$47 for the fiscal years ended June 30, 2010 and 2009, respectively. The applicable allowances for uncollectible amounts are \$45 and \$34 at June 30, 2010 and 2009, respectively. See note 5 for discussion of pledged revenue.

(f) Operating Expenses

Purchased water includes all purchases of water from the Metropolitan Water District (MWD) of Southern California and ground water basin pumping charges from the Orange County Water District (OCWD).

Treatment and pumping charges include all costs associated with the Water Utility's Lenain Filtration Plant and all costs associated with pumping the water throughout the Water Utility's water distribution system. This includes the energy costs associated with the pumps.

Operation, maintenance, and administration expenses (OM&A) include all costs associated with the distribution of water, administration, operating, and maintaining the water facilities, and customer service.

(g) Debt Issuance Costs

Debt issuance costs are deferred and amortized over the lives of the related bond issues on a basis that approximates the effective interest method.

(h) Bond Refunding Costs

Bond refunding costs are deferred and amortized over the life of the new bond or over the life of the old bond, whichever is shorter, on a basis that approximates the effective interest method. These costs are shown as a reduction of the long-term debt obligation on the accompanying financial statements.

(i) Vacation and Sick Pay

Vacation and sick pay for all City employees are paid by the General Benefits and Insurance Fund of the City. The General Benefits and Insurance Fund is reimbursed through payroll charges to the Water Utility based on estimates of benefits to be earned during the year. Vested vacation and sick pay benefits are accrued in the General Benefits and Insurance Fund and amounted to \$736 and \$670 for the Water Utility at June 30, 2010 and 2009, respectively.

**CITY OF ANAHEIM
WATER UTILITY FUND**

Notes to Financial Statements

June 30, 2010 and 2009

(In thousands)

(j) Transfers (to) from Other Funds of the City

The City Charter provides that transfers to the General Fund of the City shall not exceed 4% of total revenue. Such transfers are not in lieu of taxes and amounted to \$2,380 and \$1,978 for the fiscal years ended June 30, 2010 and 2009, respectively. In order to match the transfer's revenue base to the time period in which the revenues are earned, the Water Utility made a one-time additional \$2,084 transfer to the General Fund of the City in fiscal year 2009.

The transfer of right-of-way fees to the City represents the City Council approved transfer of 1.5% of net water revenues of the prior fiscal year to the General Fund of the City. Net revenues are defined as revenues from the sale of water, less uncollectible amounts. Bond disclosure requirements designate that this transfer must be recognized as an expense in the calculation of bond coverage. The transfer of right-of-way fee to the City amounted to \$750 and \$719 for the fiscal years ended June 30, 2010 and 2009, respectively.

Transfers from other funds of the City are either cash transfers or capital asset transfers between City funds. In fiscal year 2010, the City transferred to the Water Utility certain vehicle capital assets with a net book value of \$963. In fiscal year 2009, the City's Internal Service Funds transferred \$407 of surplus funds to Water Utility.

During the fiscal years ended June 30, 2010 and 2009, the Water Utility participated in several joint projects with the Electric Utility. The Water Utility was responsible for its share of the costs while the projects were ongoing. Upon completion, the Water Utility transferred ownership of its share of the projects to the Electric Utility, valued at \$179 and \$1,345 for fiscal years 2010 and 2009, respectively.

(k) Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of certain assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. As such, actual results could differ from those estimates.

(l) Reclassifications

Certain reclassifications have been made to the 2009 financial statement information to conform to the 2010 financial statement presentation. Such reclassifications had no effect on the previously reported change in fund net assets.

**CITY OF ANAHEIM
WATER UTILITY FUND**

Notes to Financial Statements

June 30, 2010 and 2009

(In thousands)

(2) Deposits and Investments

The City maintains a cash and investment pool, which includes the cash balances of all City funds, and is invested by the Treasurer to enhance interest earnings. The pooled interest earned, net of administrative fees, is reallocated to each fund based on average daily cash balances.

The City's pooled investment fund has been reviewed by Standard and Poor's Corporation (S&P) and received a credit rating of AAf in July 2008, which was reaffirmed in June 2010.

The City's investment policy further limits the permitted investments in Government Code Sections 53600, 16429.1, and 53684, et seq. to the following: obligations of the U.S. government, federal agencies, and government-sponsored enterprises; medium-term corporate notes; certificates of deposit; bankers' acceptances; commercial paper; LAIF; repurchase agreements; reverse repurchase agreements; and money market mutual funds.

The Water Utility maintains cash equivalents and investments at June 30, 2010 and 2009 with the following carrying amounts:

	2010	2009
Cash equivalents and investments pooled with the Treasurer	\$ 26,539	36,289
Cash equivalents and investments held with trustee	6,206	15,314
	\$ 32,745	51,603

At June 30, the Water Utility's cash equivalents and investments are recorded as follows:

	2010	2009
Restricted assets – cash equivalents and investments	\$ 10,826	20,247
Unrestricted assets – cash equivalents and investments	21,919	31,356
	\$ 32,745	51,603

(a) Investments

The Treasurer prepares an investment policy statement annually, which is presented to the Investment Advisory Commission for review and the City Council for approval. The approved investment policy statement is submitted to the California Debt and Investment Advisory Committee in accordance with Government Code.

The policy provides the basis for the management of a prudent, conservative investment program. Public funds are invested for the maximum security of principal and to meet daily cash flow needs, while providing a return. All investments are made in accordance with the

**CITY OF ANAHEIM
WATER UTILITY FUND**

Notes to Financial Statements

June 30, 2010 and 2009

(In thousands)

Government Code, and in general, the Treasurer's policy is more restrictive than Government Code.

(b) Investments Authorized by the Government Code and the City's Investment Policy

The following table identifies the investment types that are authorized for the City by its investment policy. The table also identifies certain provisions of the City's investment policy that address interest rate risk, credit risk, and concentration of credit risk. This table does not address investments of debt proceeds held by bond trustees that are governed by the provisions of debt agreements of the City, rather than the general provisions of the Government Code or the City's investment policy.

Authorized investment type	Maximum maturity	Maximum percentage of portfolio*	Maximum investment in one issue(r)	Minimum Rating (S&P/ Moody's /Fitch)
U.S. Treasury obligations	5 years	100%	30%	None
U.S. agency securities	5 years	100	40	None
Bankers' acceptances	180 days	40	5	None
Commercial paper	270 days	25	5	A-1/P-1/F-1
Negotiable certificates of deposit	360 days	25	5	None
Repurchase agreements	360 days	30	None	None
Reverse repurchase agreements	90 days	20	None	None
Medium-term corporate notes	5 years	30	5%	A/A/A
Money market mutual funds	N/A	20	10	None
LAIF	N/A	\$100 million	None	None
Time certificates of deposit (TCD)	1 year	20%	5%	None

* Excluding amounts held by bond trustees that are not subject to Government Code restrictions.

At June 30, 2010, the City exceeded 5% concentration in the following U.S. agency securities: Federal Farm Credit Bank \$52,689 (14%), Federal Home Loan Bank \$54,830 (14%), Federal Home Loan Mortgage Corporation \$33,306 (9%), and Federal National Mortgage Association \$67,857 (18%).

**CITY OF ANAHEIM
WATER UTILITY FUND**

Notes to Financial Statements

June 30, 2010 and 2009

(In thousands)

At June 30, 2009, the City exceeded 5% concentration in the following U.S. agency securities: Federal Farm Credit Bank \$53,216 (13%), Federal Home Loan Bank \$58,138 (14%), Federal Home Loan Mortgage Corporation \$77,875 (19%), and Federal National Mortgage Association \$92,289 (23%).

(c) Investments Authorized by Debt Agreements

Investment of debt proceeds held by bond trustees is governed by provisions of the debt agreements, rather than the general provisions of the Government Code or the City's investment policy. The table below identifies the investment types that are authorized for investments held by bond trustees. The table also identifies certain provisions of these debt agreements that address interest rate risk, credit risk, and concentration of credit risk.

<u>Authorized investment type</u>	<u>Maximum maturity</u>	<u>Maximum percentage of portfolio</u>	<u>Maximum investment in one issuer</u>
U.S. Treasury obligations	None	None	None
U.S. agency securities	None	None	None
Guaranteed investment contracts	None	None	None
Collateralized investment contracts	None	None	None
Flexible repurchase agreements	None	None	None
Money market mutual funds	None	None	None
LAIF	None	None	None

At June 30, 2010, the City's investments controlled by bond trustees exceeded 5% concentration in the following U.S. agency securities, guaranteed investment contracts, flexible repurchase agreements, and money market mutual funds: Federal Home Loan Bank \$49,886 (17%), Federal National Mortgage Association \$23,439 (8%), Federal Farm Credit Bank \$40,479 (13%), Bank of America \$16,645 (6%), Trinity Plus \$17,597 (6%), and Morgan Stanley \$29,931 (10%). All guaranteed investment contracts have downgrade language that requires collateral should credit ratings drop below certain levels.

At June 30, 2009, the City's investments controlled by bond trustees exceeded 5% concentration in the following U.S. agency securities, guaranteed investment contracts, flexible repurchase agreements, and money market mutual funds: Federal Home Loan Bank \$39,819 (12%), Federal Home Loan Mortgage Corporation \$22,472 (7%), Federal Farm Credit Bank \$35,838 (11%), Bank of America \$16,645 (5%), Trinity Plus \$17,597 (6%), and Morgan Stanley \$30,605 (9%). All guaranteed investment contracts have downgrade language that requires collateral should credit ratings drop below certain levels.

**CITY OF ANAHEIM
WATER UTILITY FUND**

Notes to Financial Statements

June 30, 2010 and 2009

(In thousands)

(d) Custodial Credit Risk

Custodial credit risk for investments is the risk that the City will not be able to recover the value of investment securities that are in the possession of an outside party. All securities owned by the City with the exception of LAIF and money market mutual funds are deposited in trust for safekeeping with a custodial bank different from the City's primary bank. Securities are not held in broker accounts. Funds held by LAIF and money market mutual funds are held in the City's name.

Custodial credit risk for investments held by the bond trustee is the risk that the City will not be able to recover the value of investment securities that are in the possession of an outside party. All securities held by the bond trustee are in the name of the bond issue in trust for safekeeping with the bond trustee, which is different from the City's primary bank.

(e) Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The Treasurer mitigates this risk by investing in long-term securities only with funds that are not needed for current cash flow purposes and holding these securities to maturity. The Treasurer uses the segmented time distribution method to identify and manage interest rate risk. In accordance with the City's investment policy, the Treasurer monitors the segmented time distribution of its investment portfolio and analysis of cash flow demand.

Investments held by bond trustees are typically long-term securities, which are not adversely affected by interest rate changes. Investment contracts for construction funds are usually limited to three years or less.

Information about the sensitivity of the fair values of the Water Utility's investments (including investments held by bond trustees) to market interest rate fluctuations is provided by the table on the following page.

**CITY OF ANAHEIM
WATER UTILITY FUND**

Notes to Financial Statements

June 30, 2010 and 2009

(In thousands)

The distribution of the Water Utility's proportionate share of cash and investments by maturity at June 30, 2010 and 2009 is as follows:

<u>Investments</u>	<u>Credit rating (S&P/Moody's)</u>	<u>Fair value June 30, 2010</u>	<u>12 months or less</u>	<u>13 to 24 months</u>	<u>25 to 36 months</u>	<u>37 to 60 months</u>	<u>More than 60 months</u>
Treasurer's pooled investments:							
U.S. agency securities	AAA/Aaa	\$ 14,420	3,127	2,911	3,596	4,786	—
Medium term corporate notes	AA/Aa	367	—	367	—	—	—
Medium term corporate notes	A/A	1,785	—	658	1,127	—	—
Medium term corporate notes	A-1/P-1	1,167	583	—	584	—	—
Commercial paper	A-1/P-1	4,007	4,007	—	—	—	—
Money market mutual funds	AAA/Aaa	775	775	—	—	—	—
LAIF	Unrated	4,018	4,018	—	—	—	—
Total investments controlled by City Treasurer		<u>26,539</u>	<u>12,510</u>	<u>3,936</u>	<u>5,307</u>	<u>4,786</u>	<u>—</u>
Investments controlled by bond trustees:							
Guaranteed investment agreements	Unrated	3,897	—	—	—	—	3,897
Collateralized investment contracts	Unrated	1,210	—	—	—	—	1,210
Money market mutual funds	AAA/Aaa	1,099	1,099	—	—	—	—
Total investments controlled by bond trustees		<u>6,206</u>	<u>1,099</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>5,107</u>
Total investments		<u>\$ 32,745</u>	<u>13,609</u>	<u>3,936</u>	<u>5,307</u>	<u>4,786</u>	<u>5,107</u>

<u>Investments</u>	<u>Credit rating (S&P /Moody's)</u>	<u>Fair value June 30, 2009</u>	<u>12 months or less</u>	<u>13 to 24 months</u>	<u>25 to 36 months</u>	<u>37 to 60 months</u>	<u>More than 60 months</u>
Treasurer's pooled investments:							
U.S. agency securities	AAA/Aaa	\$ 24,981	1,071	6,098	9,351	8,461	—
Medium term corporate notes	AA/Aaa	899	899	—	—	—	—
Medium term corporate notes	A/A	420	—	—	—	420	—
Medium term corporate notes	A-1/P-1	1,745	273	756	—	716	—
Commercial paper	A-1/P-1	1,597	1,597	—	—	—	—
Money market mutual funds	AAA/Aaa	6,557	6,557	—	—	—	—
LAIF	Unrated	90	90	—	—	—	—
Total investments controlled by City Treasurer		<u>36,289</u>	<u>10,487</u>	<u>6,854</u>	<u>9,351</u>	<u>9,597</u>	<u>—</u>
Investments controlled by bond trustees:							
Guaranteed investment agreements	Unrated	13,124	9,227	—	—	—	3,897
Collateralized investment contracts	Unrated	1,210	—	—	—	—	1,210
Money market mutual funds	AAA	980	980	—	—	—	—
Total investments controlled by bond trustees		<u>15,314</u>	<u>10,207</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>5,107</u>
Total investments		<u>\$ 51,603</u>	<u>20,694</u>	<u>6,854</u>	<u>9,351</u>	<u>9,597</u>	<u>5,107</u>

**CITY OF ANAHEIM
WATER UTILITY FUND**

Notes to Financial Statements

June 30, 2010 and 2009

(In thousands)

(3) Water Utility Plant

The following is a summary of changes in capital assets:

	<u>Balance as of June 30, 2008</u>	<u>Additions</u>	<u>Deletions</u>	<u>Balance as of June 30, 2009</u>	<u>Additions</u>	<u>Deletions</u>	<u>Balance as of June 30, 2010</u>
Source of water supply	\$ 35,900	1,546	—	37,446	—	—	37,446
Pumping plant	40,482	1,392	—	41,874	60	—	41,934
Transmission and distribution	217,356	28,264	(1,602)	244,018	5,936	(241)	249,713
General plant	4,908	483	(1,361)	4,030	2,271	—	6,301
Depreciable utility plant	298,646	31,685	(2,963)	327,368	8,267	(241)	335,394
Less accumulated depreciation	(88,511)	(6,918)	2,877	(92,552)	(8,103)	403	(100,252)
Net depreciable utility plant	210,135	24,767	(86)	234,816	164	162	235,142
Land	2,130	168	—	2,298	—	—	2,298
Construction in progress	21,409	31,064	(31,131)	21,342	22,045	(6,974)	36,413
Nondepreciable utility plant	23,539	31,232	(31,131)	23,640	22,045	(6,974)	38,711
Net utility plant	\$ <u>233,674</u>	<u>55,999</u>	<u>(31,217)</u>	<u>258,456</u>	<u>22,209</u>	<u>(6,812)</u>	<u>273,853</u>

(4) Operating Expenses

Total operating expenses shared with the City's Electric Utility amounted to \$27,065 and \$27,661 for the fiscal years ended June 30, 2010 and 2009, respectively, of which \$6,496 and \$5,532, respectively, of shared operating expenses were allocated to the Water Utility.

The shared expenses allocated to each utility are based on estimates of the benefits each utility derives from those common expenses.

**CITY OF ANAHEIM
WATER UTILITY FUND**

Notes to Financial Statements

June 30, 2010 and 2009

(In thousands)

(5) Long-Term Liabilities

The following is a summary of changes in long-term liabilities:

<u>June 30, 2010</u>	<u>Beginning of year</u>	<u>Additions</u>	<u>Retirements</u>	<u>End of year</u>	<u>Due within one year</u>
Water revenue bonds	\$ 54,500	—	(1,490)	53,010	880
Notes payable and advances	12,580	—	(962)	11,618	899
	67,080	\$ —	(2,452)	64,628	1,779
Less current portion	(2,452)			(1,779)	
Add unamortized bond premium	41			17	
Less unamortized refunding costs	(528)			(411)	
Total long-term liabilities	\$ <u>64,141</u>			<u>62,455</u>	
<u>June 30, 2009</u>	<u>Beginning of year</u>	<u>Additions</u>	<u>Retirements</u>	<u>End of year</u>	<u>Due within one year</u>
Water revenue bonds	\$ 7,355	48,580	(1,435)	54,500	1,490
Notes payable and advances	13,515	—	(935)	12,580	962
	20,870	\$ 48,580	(2,370)	67,080	2,452
Less current portion	(2,370)			(2,452)	
Add unamortized bond premium	122			41	
Less unamortized refunding costs	(671)			(528)	
Total long-term liabilities	\$ <u>17,951</u>			<u>64,141</u>	

**CITY OF ANAHEIM
WATER UTILITY FUND**

Notes to Financial Statements

June 30, 2010 and 2009

(In thousands)

Long-term debt consists of the following at June 30:

	2010	2009
<p>Water Revenue Bonds, 2008 Series, true interest cost (TIC) 4.8594%, dated July 1, 2008, sold on July 9, 2008 in the amount of \$48,580, maturing serially beginning October 1, 2013 through October 1, 2038. The annual principal installments range from \$260 to \$3,750 at rates ranging from 4.0000% to 5.0000%. Total remaining debt service is \$97,163 to maturity.</p>	\$ 48,580	48,580
<p>Water Revenue Bonds, 2004 Series, TIC 3.5629%, dated May 1, 2004, sold on May 26, 2004 in the amount of \$12,105, maturing serially through October 1, 2016. The annual principal installments range from \$5 to \$950 at rates ranging from 4.0000% to 4.50000%. Total remaining debt service is \$4,920 to maturity.</p>	4,430	5,920
<p>Total water revenue bonds</p>	\$ <u>53,010</u>	<u>54,500</u>
<p>Note payable to State of California Revolving Fund, interest rate of 2.8%, issued June 12, 2001, in the amount of \$18,063, semiannual principal and interest payments of \$592 through July 31, 2021; total remaining debt service is \$13,627 to maturity.</p>	\$ 11,586	12,430
<p>Advances from the OCWD, interest rate of 3.5%, a partial installment under terms of a \$750 per Well Construction Program Agreement, dated April 18, 1990, for the construction of Wells 46, 47, and 49; semiannual principal and interest installment payments of \$94 through July 31, 2010; total remaining debt service is \$32 to maturity.</p>	32	150
<p>Total notes payable and advances</p>	\$ <u>11,618</u>	<u>12,580</u>

**CITY OF ANAHEIM
WATER UTILITY FUND**

Notes to Financial Statements

June 30, 2010 and 2009

(In thousands)

Annual debt service requirements for the Water Utility's revenue bonds, notes payable, and advances at June 30, 2010 to maturity are as follows:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
Fiscal year ending June 30:			
2011	\$ 1,779	2,815	4,594
2012	1,807	2,754	4,561
2013	1,867	2,692	4,559
2014	1,742	2,629	4,371
2015	1,804	2,567	4,371
2016 – 2020	7,730	12,014	19,744
2021 – 2025	8,729	10,588	19,317
2026 – 2030	11,130	8,329	19,459
2031 – 2035	14,080	5,288	19,368
2036 – 2040	13,960	1,438	15,398
	<u>\$ 64,628</u>	<u>51,114</u>	<u>115,742</u>

Interest costs of \$1,259 and \$1,444 have been capitalized for the fiscal years ended June 30, 2010 and 2009, respectively.

In July 2008, the Water Utility issued revenue bonds in the principal amount of \$48,580. The proceeds totaled \$48,532, of which \$44,261 was deposited in project acquisition funds to finance capital improvements to the Utility's infrastructure, \$3,897 was deposited in the required reserve fund, and \$374 was used to pay for the cost of issuance. The total debt service payments over the life of the bonds until fiscal year 2039 will be \$101,195.

In accordance with the bond resolutions, a reserve for maximum annual debt service has been established and a reserve for renewal and replacement is being accumulated in an amount equal to a maximum of 1% of the depreciated book value of the utility plant in service.

The bond resolutions require the establishment of a bond service account accumulating monthly one-sixth of the interest, which will become due and payable on the outstanding bonds within the next 6 months, and by one-twelfth of the principal amount, which will mature and be payable on the outstanding bonds within the next 12 months. Those amounts have been recorded in net assets restricted for debt service on the accompanying balance sheets.

There are various limitations and restrictions contained in the Water Utility's bonds and notes. The Water Utility's management believes it is in compliance with all limitations and restrictions.

The Water Utility has pledged future revenues to repay a total of \$102,083 and \$106,117 of outstanding long-term obligations, principal, and interest for the years ended June 30, 2010 and 2009, respectively. Proceeds from bonds provide financing for various capital improvements, primarily distribution assets. The Water Utility's bonds are payable solely from water net

**CITY OF ANAHEIM
WATER UTILITY FUND**

Notes to Financial Statements

June 30, 2010 and 2009

(In thousands)

revenues and are payable through fiscal year 2039. As of June 30, 2010 and 2009, the annual principal and interest payments on the bonds are 32.1% and 26.3% of net revenues, respectively. Debt service paid and total net revenues were \$4,034 and \$12,556 and \$3,402 and \$12,916 for the years ended June 30, 2010 and 2009, respectively.

Restricted cash and investments include reserve provisions as well as undisbursed bond proceeds at June 30 as follows:

	2010	2009
Held by fiscal agent:		
Bond reserve fund	\$ 6,206	6,087
Bond construction fund	—	9,227
Held by Treasurer:		
Bond service account	1,881	2,354
Renewal and replacement account	2,739	2,579
	\$ 10,826	20,247

The Water Utility's interest and other finance charges, excluding capitalized interest, for the fiscal years ended June 30, 2010 and 2009 were \$1,746 and \$1,612, respectively.

(6) Pension Plan

The City contributes to the State of California Public Employees' Retirement System (PERS), an agent multiple-employer public employee retirement system that acts as a common investment and administrative agent for California cities that participate in this retirement plan.

For both fiscal years ended June 30, 2010 and 2009, as a condition of participation, employees are required to contribute 8% of their annual covered salary to PERS. The City pays 7% of the employees' required contributions and the employees pay the remaining 1%. The City is required to contribute the remaining amounts necessary to fund PERS, using the actuarial basis recommended by the PERS actuaries and actuarial consultants and adopted by the PERS Board of Administration. The Water Utility is allocated their portion of the City's required contribution, as determined by PERS actuaries. This allocation is based on eligible employee wages.

The Water Utility contributed \$1,298, \$1,011, and \$911 to PERS for the fiscal years ended June 30, 2010, 2009, and 2008, respectively, which represented 100% of its required contributions.

Information is not available separately for the Water Utility as to the cost of benefits funded, the actuarially computed present value of vested and nonvested accumulated plan benefits, the related assumed rates of return used, and the actuarially computed value of vested benefits over the related pension fund assets. Refer to the City's Comprehensive Annual Financial Report as of June 30, 2010 for further information.

**CITY OF ANAHEIM
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June 30, 2010 and 2009

(In thousands)

(7) Self-Insurance Program

The Water Utility participates in the City's self-insured workers' compensation and general liability program. The liability for such claims, including claims incurred but not reported, is transferred to the City in consideration of self-insurance premiums paid by the Water Utility. Premiums for workers' compensation and general liability programs are charged to the Water Utility by the City based on various allocation methods that include actual cost, claims experience, exposure base, and number of participants. Premiums charged and paid were \$150 and \$89 for the fiscal years ended June 30, 2010 and 2009, respectively.

At June 30, 2010, the City was fully funded for self-insured workers' compensation and general liability claims (self-insured retention levels of \$750 per occurrence for workers' compensation claims and \$1,000 per occurrence for general liability claims). Above these self-insured retention levels, the City's potential liability is covered through various commercial insurance and intergovernmental risk pooling programs. Settled claims have not exceeded total insurance coverage in any of the past three years, nor does management believe that there are any claims pending that will exceed total insurance coverage.

(8) Regulatory Credits

The Water Utility's Rates, Rules, and Regulations provide for a water regulatory credits account to reflect variations in the cost of water to the Water Utility and provide more stable retail water rates to the customers of the City's Water Utility. This rate stabilization account (RSA) provides increased flexibility by allowing the Water Utility to maintain financial performance indicators and goals specified in bond covenants. The account is funded through expense reimbursements such as water supply cost refunds received from the MWD and OCWD and other miscellaneous credits and revenue. As permitted by FASB Statement No. 71, *Accounting for the Effects of Certain Types of Regulation*, and approved by the City Council, revenues from amounts collected are deferred and recorded as regulatory credits in the balance sheets. At June 30, 2010 and 2009, the liability recorded for regulatory credits totaled \$5,937 and \$7,157, respectively. In fiscal years 2010 and 2009, the Water Utility funded this account through a variety of miscellaneous credits. During fiscal year 2010, \$1,300 was recognized as RSA revenue to mitigate the impact of water supply costs. During fiscal year 2009, no RSA revenue was recognized.

(9) Commitment and Contingencies

(a) Litigation

A number of claims and suits are pending against the City for alleged damages to persons and property and for other alleged liabilities arising out of matters usually incidental to the operation of a utility such as the water system of the City. In the opinion of management, the exposure under these claims and suits would not materially affect the financial position of the Water Utility as of June 30, 2010 and 2009.

**CITY OF ANAHEIM
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June 30, 2010 and 2009

(In thousands)

(b) Construction Commitments

At June 30, 2010, the Water Utility had the following commitments with respect to unfinished capital projects:

<u>Capital project</u>	<u>Construction commitment</u>	<u>Estimated completion date</u>
Well #54 next to Anaheim Substation	\$ 540	2010
Well #56 at Willow Park	808	2011
Parkview Pump Station Upgrade	535	2010
Nohl Canyon Tank	428	2010
	<u>\$ 2,311</u>	

At June 30, 2009, the Water Utility had construction commitments totaling \$11,566.

(10) Subsequent Events

On October 28, 2010, the Water Utility received the proceeds from the sale of the Anaheim Public Financing Authority (Authority) Revenue Bonds, 2010-A Series (Tax Exempt), TIC 2.19%, dated October 28, 2010 in the amount of \$4,835, maturing serially through October 1, 2021 and also, the proceeds from the sale of the Authority's Revenue Bonds 2010-B Series (Federally Taxable Build America Bonds), TIC 3.64%, dated October 28, 2010 in the amount of \$29,690, maturing serially through October 1, 2040. The annual principal installments, which begin June 30, 2014, range from \$120 to \$5,645 at rates ranging from 2.00% to 5.70%. The bonds were issued by the Authority for the purpose of providing financing for the acquisition and construction of new storage facilities, wells, pumping facilities and various other capital projects of the Water utility. The revenues of the Water Utility have been pledged to pay this long-term obligation.